#### STATE OF IOWA

#### DEPARTMENT OF COMMERCE

#### **UTILITIES BOARD**

IN RE:

U S WEST COMMUNICATIONS, INC., AND CITIZENS TELECOMMUNICATIONS COMPANY OF IOWA DOCKET NOS. SPU-99-31 WRU-00-29-3047

#### **ORDER**

(Issued April 28, 2000)

On November 9, 1999, U S WEST Communications, Inc. (U S WEST), and Citizens Telecommunications Company of Iowa (Citizens) (collectively, the Applicants) filed a joint application with the Utilities Board (Board) for (1) approval of reorganization, (2) discontinuance of service by U S WEST, (3) transfer of certificate of public convenience and necessity for the exchanges involved, (4) transfer of interexchange service of U S WEST to Citizens for the exchanges involved, (5) waiver of the slamming rule, 199 IAC 22.23, if necessary, (6) designation of Citizens as an Eligible Telecommunications Carrier (ETC) in each of the exchanges involved, and (7) assumption by Citizens of the U S WEST price plan at the rates in effect at the date of close for the exchanges involved, pursuant to Iowa Code §§ 476.77, 476.20, and 476.29 (1999). Additionally, the Applicants requested that the Board order state that it did not object to the FCC granting study area waivers or to any reconfiguration of study area boundaries for the Iowa exchanges involved in the reorganization. The underlying transaction involves the sale of 32

U S West exchanges to Citizens. The Board identified the joint application as Docket No. SPU-99-31 and the slamming rule waiver as Docket No. WRU-00-29-3047.

On November 15, 1999, the Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed an answer and a motion to extend the 90-day review period by an additional 90 days, pursuant to Iowa Code § 476.77(2). The Board set the application for hearing, extending the review period by 90 days, and set a procedural schedule for this docket by an order dated December 16, 1999.

On December 13, 1999, AT&T Communications of the Midwest, Inc. (AT&T), filed a petition to intervene. The Board granted intervention to AT&T by an order dated December 30, 1999.

On January 31, 2000, U S WEST and Citizens filed a request for an extension of time to file prepared rebuttal testimony, with supporting exhibits and work-papers. According to the request, U S WEST personnel who would participate in the preparation of the rebuttal testimony were also engaged in the U S WEST and Qwest Inc. merger proceeding (Docket No. SPU-99-27). Because of hearings commencing on February 1, 2000, in that proceeding, those personnel did not have adequate time and resources to prepare necessary rebuttal testimony for filing on February 4, 2000. The Board granted an extension of time to file rebuttal testimony until February 9, 2000.

On February 23, 2000, the Applicants and the Consumer Advocate filed a proposed settlement agreement and a joint motion for approval of the agreement.

The proposed settlement was intended to resolve all issues between the Applicants and Consumer Advocate, except the issue concerning the acquisition premium to be paid by Citizens. The only other party to this docket, AT&T, was not a party to the proposed settlement.

Comments contesting all or part of the proposed settlement were ordered to be prepared for filing at the hearing scheduled for February 29, 2000, pursuant to the Board's February 25, 2000, order. Additionally, the Board required responses to additional questions based on the partial settlement agreement to be presented at the hearing on February 29, 2000, if possible. Any information not available at the hearing on February 29, 2000 was to be filed no later than March 6, 2000.

On February 29, 2000, the hearing on the application opened as scheduled. Following discussion on procedural matters, the hearing was continued. The hearing on the application and the partial settlement continued on March 29, 2000, at which time the witnesses were made available for cross-examination on the prefiled testimony entered into the evidentiary record and for questions related to the partial settlement agreement. Briefs were filed by Applicants and Consumer Advocate on April 10 and 17, 2000.

Iowa Code § 476.77(3) states:

- 3. In its review of a proposal for reorganization, the board may consider all of the following:
- a. Whether the board will have reasonable access to books, records, documents, and other information relating to the public utility or any of its affiliates.
- b. Whether the public utility's ability to attract capital on reasonable terms, including the maintenance of a reasonable capital structure, is impaired.

- c. Whether the ability of the public utility to provide safe, reasonable, and adequate service is impaired.
  - d. Whether the ratepayers are detrimentally affected.
  - e. Whether the public interest is detrimentally affected.

The Board will consider each of these factors in this order.

## A. WHETHER THE BOARD WILL HAVE REASONABLE ACCESS TO BOOKS, RECORDS, DOCUMENTS, AND OTHER INFORMATION RELATING TO THE PUBLIC UTILITY OR ANY OF ITS AFFILIATES

Citizens will maintain its books and records at the Citizens headquarters located at 5600 Headquarters Drive, Plano, Texas. (Tr. 11) Citizens has stated its assurance that appropriate access to the books and records will be made to the board and its staff. (Tr. 181-82) Because of this assurance, if the reorganization is not disapproved, the Board will waive the requirement of 199 IAC 18.2 that all records required by the Board's rules be kept within the state of Iowa.

There is no mention of this statutory factor, nor is there any discussion about the location the records of Citizens, in the partial settlement agreement filed February 23, 2000, with the Board. The Board's finding that this factor, and other factors, have been met must be based upon the entire record as cited above and not merely the partial settlement agreement.

# B. WHETHER THE PUBLIC UTILITY'S ABILITY TO ATTRACT CAPITAL ON REASONABLE TERMS, INCLUDING THE MAINTENANCE OF A REASONABLE CAPITAL STRUCTURE, IS IMPAIRED

Because U S WEST will continue to provide service in Iowa even if the reorganization is approved and completed, the Board must consider the effect of this sale on the financial strength of U S WEST as well as the financial strength of Citizens. According to testimony, the effect of the sale of these 32 exchanges is very

small considering U S WEST's total holdings in Iowa and as a whole. (Tr. 88) The effect on U S WEST's capital structure should be minimal according to this testimony, with no material impact on U S WEST's ability to attract capital or to maintain a reasonable capital structure.

Citizens' capital structure will initially consist of 100 percent common equity.

(Tr. 9) Although this capital structure has no financial risk, it does not take advantage of the benefits of using debt. Since Citizens will be operating under U S WEST's price plan, the ratepayers will be protected from this less than optimal capital structure. The Board may address this issue in future rate case proceedings, if necessary.

Also, according to testimony, Citizens will not operate as a stand-alone company. The parent will be providing Citizens' financing. Even though Citizens does not have current plans to issue any debt, the possibility is not precluded. (Tr. 315-18).

The Board also considered the financial strength of the parent company,
Citizens Utilities Company. As demonstrated by the record, Citizens Utilities
Company is financially strong and has strong investment grade ratings on debt. The applicants' belief that no additional debt is needed to complete this transaction further supports the stability of Citizens Utilities Company's capital structure. (Tr. 123)

There is no mention of this statutory factor in the partial settlement agreement filed February 23, 2000. The Board's finding that this factor, and other factors, have

been met must be based upon the entire record as cited above and not merely the partial settlement agreement.

### C. WHETHER THE ABILITY OF THE PUBLIC UTILITY TO PROVIDE SAFE, REASONABLE, AND ADEQUATE SERVICE IS IMPAIRED

The partial settlement agreement contains a number of provisions relating to Citizens' ability to provide safe, reasonable, and adequate service. (See e.g. Paragraphs 2-11) However, as with the previous factors, the Board will consider the entire record in analyzing this factor. That appears to be the intent of the Joint Applicants in that they, too, relied on the entire record, not just the partial settlement, in making their arguments. (See p. 17, Joint Applicants' Initial Brief, filed April 10, 2000)

Citizens has stated expressly it has no reservation about committing to meet the Board's quality of service rules within one year of taking possession of the exchanges. (Tr. 209) Based on confidential information filed by U S WEST in this docket concerning existing conditions with respect to service quality, it is clear that service has not been in compliance with these rules in all respects. Therefore, Citizens' express commitment with respect to these rules will enhance service quality in these exchanges.

There exist varying levels of commitment and ambiguity in several areas among the application, prefiled testimony, hearing testimony, briefs and express provisions in the partial settlement.

The partial settlement sets targets for held orders for primary service of levels not to exceed 1.0 percent of service orders, based on a three-month rolling average

of held orders longer than thirty 30 days. The standard in the partial settlement is based on the settlement commitments in the U S WEST/Qwest merger transaction and does not relate to conditions specific to these exchanges. (Tr. 396). The Board's rules do not set an explicit level. The 1.0 percent standard appears to be inconsistent with paragraph two of the partial settlement which asserts, fully and without reservation, that the quality and reliability of all services shall in all respects and at all times following consummation of the transaction be preserved or enhanced. The record shows that during 1998 and 1999, held order levels never exceeded .5 percent of service orders, and that application of a 1 percent standard would authorize held order levels at double these historic highs. (Tr. 394) The question of whether safe, reasonable and adequate service will be impaired if the reorganization is allowed to go forward cannot be answered in the affirmative if the partial settlement authorizes held order levels beyond historic levels. To give effect to Citizens' unqualified commitment to preserve or enhance quality of service, held order levels cannot exceed .5 percent. In fact, these held orders have been very low in recent months. Even a standard of .5 percent exceeds recent performance by U S WEST in these exchanges.

There is ambiguity with respect to investment commitment. Paragraph ten of the partial settlement establishes an average investment per line of \$90. However, this amount appears to be only a portion of the total, which Citizens estimates will be approximately 30 million dollars over the first four years. (Initial brief p. 16) If the Board relies on assertions and arguments made by Citizens, then the \$90 per line in

the settlement must be interpreted as only a portion of the total investment contemplated for these exchanges. (See also Tr. 186, 363-65)

The Board understands that it is Citizens' intent to comply fully with Board service quality rules. It is the Board's belief that Citizens also intends to comply with the most rigorous commitments relied on by Citizens in support of this reorganization proceeding: the initial filing, the record, the partial settlement, and the briefs. The parties to the partial settlement agreement will be required to affirm the Board's understanding of the commitments supporting this reorganization or identify the commitments they will not be able to honor on or before May 1, 2000. If all commitments are not affirmed, the Board will reevaluate this factor and its impact on the Board's final decision in this reorganization in light of the response.

#### D. AFFECT ON RATEPAYERS

Applicants assert that the reorganization will be reasonably transparent to the ratepayers, and that over time will have beneficial effects on lowa ratepayers because it is expected to produce a more customer-focused and efficient company. Citizen's requests that it be permitted to adopt U S WEST's local service rates and charges and the U S WEST price plan. (Tr. 125) Citizens also has agreed that it will adopt U S WEST's long distance and access rates and will provide interconnection service under existing U S WEST agreements, if other agreements are not mutually reached with the carriers. (Tr. 126) Citizens will provide the same products and services to the customers as U S WEST currently provides in the 32 affected exchanges. (Tr. 185)

U S WEST witness Phillips agreed to provide information to the Board detailing how many extended area service (EAS) routes are within these 32 exchanges; how many EAS routes have had petitions approved but not yet proceeded to balloting; and how many petitions have proceeded through balloting and received adequate votes, but not yet been implemented. (Tr. 275-76) The Board has not received that information and will direct U S WEST to provide the information by no later than May 1, 2000.

Consumer Advocate reserved for litigation all issues surrounding the acquisition premium in paragraph 14. This is a rate case issue best left for argument in a future rate case or other appropriate proceeding.

If the service quality commitments discussed in the previous section are forthcoming and no problem is identified with the EAS routes, the Board will be able to find that this factor is satisfied.

#### E. EFFECT ON THE PUBLIC INTEREST

The final statutory consideration listed in Iowa Code § 476.77(3) is whether the public interest is detrimentally affected by the proposed reorganization. Each of the paragraphs of the partial settlement agreement was reviewed by the Board as having some effect on the public interest. However, the issue of "public interest" includes a broader set of concerns and the Board must consider the impact of the proposed reorganization as a whole, on the entire state.

The Board is encouraged that the employees of U S WEST will have the option of other positions or duties within U S WEST if they do not become employees of

Citizens. (Tr. 50-51) Additionally, Citizens anticipates a need to hire additional employees in the state of lowa to serve the acquired exchanges. (Tr. 119, 181, 287-88)

The Board finds the adoption by Citizens of the price plan of U S WEST, which will continue in effect until November 2001, to be in the public interest. (Tr. 50, 129)

Citizens will then have the option to continue the plan for another three years.

The public will also benefit from Citizens' ability to package long distance service with local service and receive both services from one provider if the customer chooses to do so.

Finally, the Board notes that Citizens has always participated within each community served through sponsorship and participation in activities associated with various civic organizations and encourages its employees to participate in volunteer and charitable activities. (Tr. 131)

If the commitments discussed in the previous sections are forthcoming, the Board will be able to find that this factor is satisfied.

#### CONCLUSION

This is not the final order of the Board in this docket. However, it does contain a discussion of each of the factors. If the parties affirm the Board's understanding that the parties to the partial settlement are bound by the most rigorous commitments made at any point in the record in this case and not just those in the partial settlement, then the Board will be able to issue an order that approves the partial settlement and that does not disapprove the reorganization. If the parties to

the partial settlement do not affirm that understanding, the Board will determine whether to disapprove the reorganization on this record.

#### OTHER MATTERS

As indicated in the first paragraph of this order, there are several other matters that the Applicants have asked the Board to address as a part of this reorganization review. These, and any other issues, will be discussed in a subsequent order, if necessary.

#### **ORDERING CLAUSES**

#### IT IS THEREFORE ORDERED:

1. It is the Board's understanding that the parties to the partial settlement intend to be bound by the most rigorous commitments made at any point in the record in this case and not just those in the partial settlement. On or before May 1, 2000, the parties to the Partial Settlement Agreement shall file a statement that they agree with the Board's understanding. If the parties cannot affirm this level of commitment they shall specify the commitments that they choose not to honor.

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2. U S WEST is directed to file the EAS information as specified in this order no later than May 1, 2000.

	UTILITIES BOARD
	/s/ Allan T. Thoms
ATTEST:	/s/ Susan J. Frye
/s/ Judi K. Cooper Executive Secretary, Deputy	/s/ Diane Munns

Dated at Des Moines, Iowa, this 28<sup>th</sup> day of April, 2000.